BEFORE THE

SURFACE TRANSPORTATION BOARD

2.15 36

FINANCE DOCKET NO. 35506

WESTERN COAL TRAFFIC LEAGUE – PETITION FOR DECLARATORY ORDER

REBUTTAL COMMENTS OF
ALLIANCE FOR RAIL COMPETITION
MONTANA WHEAT & BARLEY COMMITTEE
COLORADO WHEAT ADMINISTRATIVE COMMITTEE
IDAHO BARLEY COMMISSION
IDAHO WHEAT COMMISSION
MONTANA FARMERS UNION
NEBRASKA WHEAT BOARD
OKLAHOMA WHEAT COMMISSION
SOUTH DAKOTA WHEAT COMMISSION
TEXAS WHEAT PRODUCER BOARD
WASHINGTON GRAIN COMMISSION
NATIONAL ASSOCIATION OF WHEAT GROWERS

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Dated: December 20, 2011

These rebuttal comments are hereby filed by the Alliance for Rail Competition ("ARC"). on behalf of its captive shipper members, whose freight includes coal, agricultural and other commodities, along with the agricultural interests listed on the cover (collectively, "ARC, et al.").

At this rebuttal round of this proceeding, it is appropriate to focus on the most important of BNSF's erroneous claims. In the judgment of ARC, et al., this is BNSF's claim that if the Board treats the Berkshire Hathaway acquisition premium as acquisition premiums have been treated in past cases involving acquisition of a Class I railroad, there will be no adverse impacts on shippers.

ARC, et al. do not mean to suggest that this is BNSF's only error. We agree with WCTL and other shipper parties that BNSF's arguments calling on the Board to follow what BNSF regards as binding precedent are specious. This acquisition clearly differs from previous acquisitions in many respects. For one thing, in past acquisitions, the acquiring railroad received the benefits of a costing adjustment based on its expenditures. Here, the acquisition premium was paid by Berkshire Hathaway, but BNSF, as acquiree, seeks the benefit.

In addition, prior acquisitions took place in an environment of concerns (whether overblown or not) about the railroad industry's financial health, and ICC and STB reluctance to discourage acquisition of weaker railroads by stronger ones. Today, there can be no serious doubt about the financial strength of BNSF, and the last major action by the agency in the context of an acquisition or potential acquisition of a Class I railroad was the 15 month moratorium on mergers imposed by the Board in 2000. That moratorium was prompted by BNSF's plan to acquire CN, and fears that the result would be acquisitions producing a North American railroad duopoly.

More broadly, captive shippers are increasingly concerned about efforts by major railroads to weaken or evade effective rate regulation by the STB. These efforts have taken various forms, but include railroad efforts to redefine jurisdictional common carrier service as non-jurisdictional contract service; efforts to persuade the Board that potential or even actual service by more than one railroad equates to "effective competition" and an absence of market dominance; shipments size limits like those challenged in State of Montana v. BNSF, STB Docket No. 42124; and the increasing use of charges and practices to impose costs and burdens on captive shippers, for which the recourse, if any, is generally limited to an unreasonable practice challenge.

Certainly, the URCS treatment of the acquisition premium that BNSF argues for in this proceeding is another reason for concern by captive shippers. If Berkshire Hathaway can pay billions of dollars more than the market capitalization of BNSF, and enjoy a write-up of its URCS costs, and an across-the-board reduction in R/VC percentages, so can the acquirer of NS, CSX or UP. Indeed, the resulting windfall will make such acquisitions more attractive, which is likely to result in higher acquisition premiums and greater reductions in regulatory recourse for captive shippers on those railroads. The time for the Board to take corrective action is now.

These considerations would warrant new approaches even if BNSF were correct in claiming that captive shippers will be unaffected, but it is not correct. At page 12 of its Reply Comments, BNSF notes that the "overwhelming majority" of its rates are not subject to STB regulation. This is true but irrelevant. The focus of this proceeding is, or should be, the impact of the acquisition premium of captive shippers' rates, because those are the only rates over which the Board has jurisdiction.[1]

BNSF goes on to argue that it ignores its own "rate base" in setting rates. As shown by extensive evidence in the opening and reply rounds, R/VC percentages are not irrelevant to BNSF in setting rates, even if the railroad is unrestrained by extraordinarily high R/VC levels. More to the point, however, is the importance of R/VCs to captive shippers assessing their options when faced with high BNSF rail rates and rate increases.

Given the high cost and technical complexity of assessing rate levels using SAC, SSAC or the Three Benchmark test, captive shippers look at R/VC percentages in judging whether they have any hope of obtaining relief, either in a rate case or through negotiations. Some shippers assess the extent to which rates exceed 180% of variable costs. Others use a more conservative approach, considering how far above 200% or 220% the R/VC percentages are. For all of these shippers, artificial increases in costs producing reductions in R/VC percentages mean BNSF rates and rate increases that, as a legal or practical matter, will not be challenged. BNSF benefits and captive shippers are harmed.

And, of course, the actual costs of services BNSF is providing have not risen because of the Berkshire Hathaway acquisition. Indeed, some costs may have been reduced because BNSF is no longer publicly held. In their Study of Competition in the U.S. Freight Railroad Industry, Christensen Associates found that rail rate increases may have been justified because reflective of cost increases rather than increasing abuse of market power. Assuming there is validity in these conclusions to the extent that captive shippers are not disproportionately affected, the cor-

[1] If virtually all BNSF rates will necessarily be unaffected because they are non-jurisdictional, why is BNSF arguing so vigorously (and without evident support from Berkshire Hathaway) against URCS cost adjustments that would maintain the status quo as to captive shippers?

ollary must be that rate increases without costs increases are appropriate matters for regulatory and shipper concern.

BNSF acknowledges that shippers using the Three Benchmark test will lose regulatory protections due to artificially increased RSAM numbers, but brushes aside ARC's concerns about widespread adverse impacts. Notably, BNSF simply ignores ARC's comments that Three Benchmark is the test most likely to be used by smaller shippers and producers of agricultural commodities, and that such entities are particularly vulnerable to the abuse of railroad market power.

BNSF is dismissive of ARC's observations about market dominance, but these concerns are squarely based in the realities of western rail transportation of wheat, barley, corn and other agricultural commodities. Montana, in particular, is almost completely captive to BNSF, which controls over 90% of wheat shipments. Large portions of other states served by BNSF are equally captive.

Moreover, based on recent history, ARC cannot accept as "histrionic" the prospect of further rate increases to take advantage of BNSF's heightened immunity from rate case challenges. BNSF rate increases on western shipments of agricultural commodities have been frequent and substantial. Moreover, the relatively small size of many agricultural shippers and producers and the competitiveness of the market mean that a succession of even modest rate increases can undermine these companies' businesses.[2]

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[2] BNSF criticizes ARC Witness Fauth's calculations, but Mr. Fauth explained that his estimate was based on STB indexing procedures, and that actual amounts would need to be based on 2010 URCS costs. Those costs were just released on December 9, 2011.

For the forgoing reasons, the Board should exclude the acquisition premium from BNSF's URCS costs, and exclude the premium for revenue adequacy purposes.

Respectfully submitted,

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Dated: December 20, 2011

CERTIFICATE OF SERVICE

I hereby certify that I have this 20th day of December, 2011, caused copies of the foregoing document to be served on all parties of record by first-class mail.

John M. Cutler, Jr.

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